extendicare ltd.

annual report

1978

a decade of service: 1968/1978

FINANCIAL HIGHLIGHTS — extendicare ltd.

	Fiscal year ended August 31				
	1978	1977	1976	1975	1974
Revenues					
Skilled Nursing Centres	**$52,511,850**	$42,007,864	$27,152,994	$22,893,296	$17,740,024
Medical, Surgical, Pharmaceutical Supplies and Equipment	**26,800,787**	23,049,244	21,346,099	22,679,600	13,192,166
Diagnostic Centres and other	**8,008,216**	6,117,376	5,393,957	3,386,475	3,407,829
Total Revenues	**87,320,853**	71,174,484	53,893,050	48,959,371	34,340,019
Before extraordinary items					
Earnings	**3,138,052**	2,689,685	2,248,805	1,900,553	1,318,028
Earnings per share	**1.52**	1.32	1.12	0.96	0.80
Dividends paid per share	**0.33**	0.26	0.22	0.18	0.11
Total Assets	**69,914,426**	64,857,554	46,523,212	45,980,175	41,933,178
Shareholders equity	**17,871,809**	13,692,968	11,424,385	9,258,440	7,646,154
Weighted average number of shares outstanding	**2,064,507**	2,037,640	2,007,862	1,979,742	1,647,535

CHAIRMAN'S MESSAGE

To our shareholders:

This annual report marks our 10th year as a public company. The expansion of Extendicare as a prominent presence in the health care field over these past 10 years reflects both the growing demand for high levels of care at a reasonable cost and our ability to meet this demand through a variety of essential services delivered with proficiency and professionalism.

It is worth recalling that at the end of our first fiscal year, Extendicare operated one nursing centre with 103 beds, had four under construction and had total assets of just over $7 million.

By the close of our 10th year of operation, our assets have grown to just under $70 million, the number of facilities we own, lease or manage to 51 (including a 120 bed facility under construction in Newburgh, Indiana), the number of operational beds to 6,260 and the number of annual patient days of extended care to 2,197,019.

In fiscal 1978, Extendicare had consolidated revenue of $87,320,853, in comparison with $71,174,484 for the same period the previous year. Net earnings were $3,138,052 or $1.52 per share, an increase over fiscal 1977 net earnings of $2,689,685 or $1.32 per share.

On January 15, 1979, the company was continued under the Canada Business Corporations Act. Each common share of Extendicare has been sub-divided into one non-voting Class A share and one convertible common share. The Class A shares have an additional annual preferential dividend of ten cents per share payable in equal quarterly instalments. The common shares are convertible into Class A shares on a share for share basis.

The past decade has witnessed a maturing of the health care field. Governments, investors in public companies and major private firms have accepted their roles and responsibilities of ensuring a high standard of health care.

From our solid base of people and resources, I am confident that Extendicare will continue to enjoy satisfactory growth in earnings and influence. Our direction in the future will be in the geographical expansion of our operations within two major areas: (1) through ownership and management of more nursing centres and hospitals, and (2) through ownership of more clinical laboratories.

The opportunities have never been greater for Extendicare to apply its expertise. The complex management problems facing health care delivery today underscore the need for our services and systems. Thus, we have been vigorously developing the important area of providing our multi-unit management services to public and private organizations and governments. The company has also developed a consulting division, consisting of professionals having a broad spectrum of skills and practical experience to act as an independent advisor and an objective resource.

Discussions have been progressing for management of health care facilities in North America. During the past fiscal year, Extendicare also entered into discussions in Europe and submitted proposals in the Middle East, to manage hospitals.

In the past year, increased interest in our services has prompted us to establish a presence in Alberta and British Columbia. The company also renewed, for another five years, its agreement to manage a chronic care hospital, the only hospital in Canada to be managed under contract.

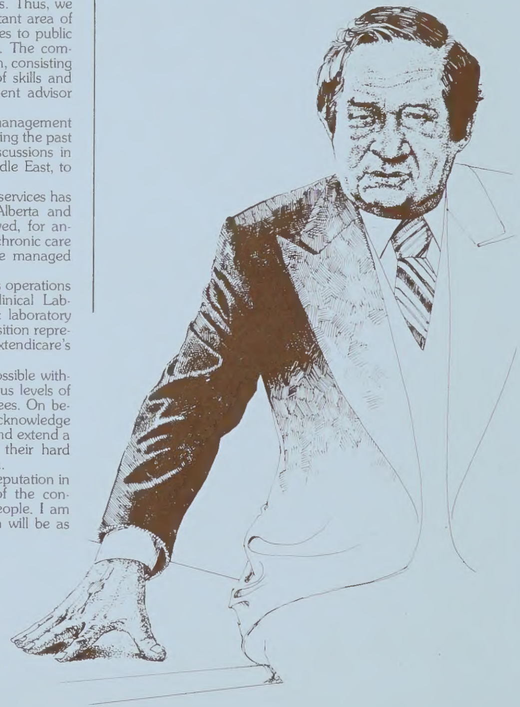
In fiscal 1978, we expanded United States operations through the acquisition of Professional Clinical Laboratories, Inc., the largest private diagnostic laboratory company in the state of Delaware. This acquisition represents a further geographical expansion of Extendicare's areas of operation.

Our continuing success would not be possible without the confidence and cooperation of various levels of governments, our shareholders and employees. On behalf of the Board of Directors, I gratefully acknowledge the support of these individuals and groups and extend a special appreciation to our employees for their hard work, dedication, imagination and enthusiasm.

Extendicare is proud of its standing and reputation in the growth field that is health care, and of the contribution we are making to the health of people. I am confident that our next decade of operation will be as rewarding and exciting as the first 10 years.

H. L. Livergant

January 15, 1979



5-YEAR STATISTICAL AND FINANCIAL HIGHLIGHTS/ extendicare ltd.

Number of Operational Beds

1978	6,260
1977	6,429
1976	3,784
1975	3,912
1974	3,412

Total Patient Days

1978	2,197,019
1977	1,949,714
1976	1,340,913
1975	1,160,179
1974	1,068,580

Number of Employees

1978	5,100
1977	5,075
1976	3,255
1975	3,021
1974	2,650

Revenues

1978	$87,320,853
1977	$71,174,484
1976	$53,893,050
1975	$48,959,371
1974	$34,340,019

Earnings Per Share Before Extraordinary Items

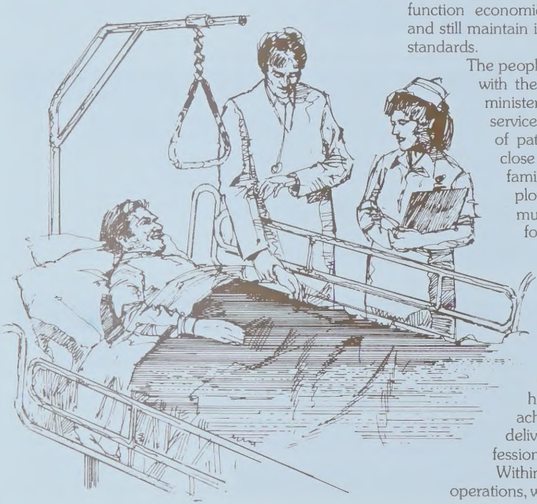
1978	$1.52
1977	$1.32
1976	$1.12
1975	$ .96
1974	$ .80

Total Assets

1978	$69,914,426
1977	$64,857,554
1976	$46,523,212
1975	$45,980,175
1974	$41,933,178

MEETING THE NEED FOR EFFECTIVE HEALTH CARE SERVICES

Throughout the ten years of our existence, we at Extendicare have been dedicated to providing high quality health care at an economical cost. We have been able to attain effective delivery of health care services primarily because we have a skilled and experienced team of professionals functioning in a multi-unit management setting. The development of this strategy has been in direct response to numerous pressures — inflation and fiscal restraints, medical technological expansion, innovations in patient care, greater demands made by consumers, physicians, unions, government and patients — all of which have made it more and more difficult for the health care system to function economically and still maintain its high standards.



The people charged with the responsibility for planning, administering and delivering health care services must clearly identify the needs of patients or residents and work in close cooperation with the residents' families, the physicians, the employees and the community. They must strive to gain optimum value for every health care dollar spent.

At Extendicare, it is our conviction, based on extensive practical experience, that the care of people is dependent on concern for the individual, well-directed therapeutic programs and skills, and quality support services. These goals, however, can only be optimally achieved if the environment and delivery program is completely professional.

Within Extendicare's own multi-unit operations, we have the scope and leadership which allows us to attract and utilize top managers, health care specialists and back-up resources. All of these help us deliver more effective institutional and non-institutional health care to people.

Extendicare believes that our experience and resources can be of assistance to others in helping to solve complex health care problems. Increasingly, we are providing professional health care management services and consulting services to a broad range of governments and organizations involved in health care delivery. Extendicare also provides knowledgeable consulting services to governments and others, acting as an independent resource and technical advisor on in-depth studies and projects in many areas of health care.

The growth in size and prominence of Extendicare is thus a direct result of our ability to provide effective health care delivery, as well as a variety of management and consulting services, wherever needed.

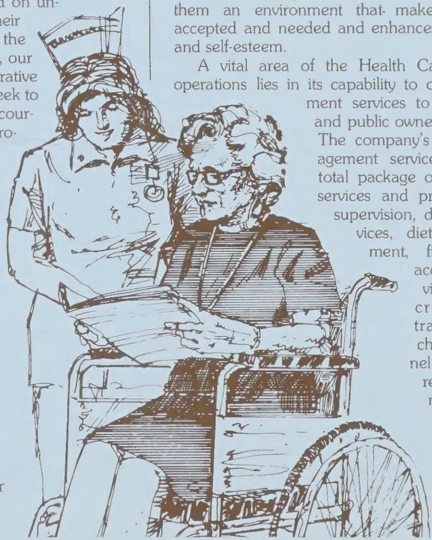
HEALTH CARE OPERATIONS — CANADA

HEALTH CARE FACILITIES

The philosophy of Extendicare's Skilled Nursing Centres is that the residents of the centre must retain contact with the community and must receive the best possible comprehensive care, assurance of their safety and comfort through effective management, and a high degree of professional service that is based on understanding and concern for their individual needs. Operated by the company's Health Care Division, our nursing centres emphasize restorative rather than custodial care, and seek to provide an atmosphere that encourages participation in activity programs and strong communication with families, volunteer workers and the local community. The accent on lifestyle for residents is promoted through planned activities, such as concerts, social evenings, excursions, handicrafts, and therapeutic programs to help maintain individuality.

An interdisciplinary team approach is used within each Extendicare facility. The steps in this approach include continued assessment of each resident's needs and the development of a comprehensive program to meet these requirements. The team responsible for implementing each step of this program consists of the administrator, the director of resident care, and a trained health care and support staff. All are backed up by the experience and expertise of Extendicare's many resource consultants. Also available to the team are the technical and management skills of the total organization.

Extendicare's staff members in each centre have a continuing two-fold goal: to provide the residents with high quality care and to create for them an environment that makes them feel accepted and needed and enhances their dignity and self-esteem.



A vital area of the Health Care Division's operations lies in its capability to offer management services to both private and public owners of facilities. The company's facility management services provide a total package of health care services and programs: staff supervision, diagnostic services, dietary management, financial and accounting services, staff recruiting and training, purchasing, personnel and labour relations, engineering and maintenance, day care and all phases of facility design, financing, construction and management. The company is also able to help other organizations and institutions devise and develop programs and facilities employing any or all of these services to meet particular health care needs.

Extendicare currently owns, leases or manages 25 facilities in Canada, representing 3,921 licensed beds. The number of patient days in fiscal 1978 totalled 1,450,457.

Augmenting the Skilled Nursing Centre services are the day care programs for the aged in some facilities. Expert care, companionship and a stimulting environment are important catalysts for aiding the physical condition of the elderly and for meeting their spiritual and emotional needs. There is a growing requirement in our society for a service which provides these benefits without displacing elderly persons from their present social and physical environment. The day care program makes it possible for elderly citizens to remain in their own homes or with families.

DIAGNOSTIC SERVICES

Extendicare believes strongly in the contribution of clinical health care. Diagnostic service benefits support the preventive aspects of health care by providing early detection of health care problems.

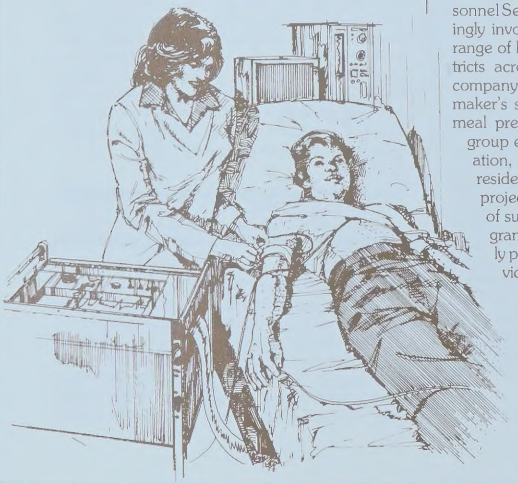
The network of medical laboratories operated by the company's Diagnostic Services Division in Metropolitan Toronto performed over two million clinical tests during the past year. As an integral part of effective health care delivery, this division

carries out laboratory procedures and analyses for diagnosis, treatment and prognosis of disease and for the maintenance of health.

Extendicare's laboratories, staffed by professionally trained technologists working with up-to-date scientific equipment, perform a comprehensive range of tests. Stringent quality standards and an 18-hours-a-day, six-days-a-week service provide responsive and accurate testing and reporting.

The Diagnostic Services Division is expanding its operations by offering many of its services on site. This includes pulmonary function studies at various locations and portable ECG units.

In the future, the division expects to have mobile multi-phasic screening units operating in Canada to bring medical tests to people in community locations who are unable to obtain transportation to a laboratory site.



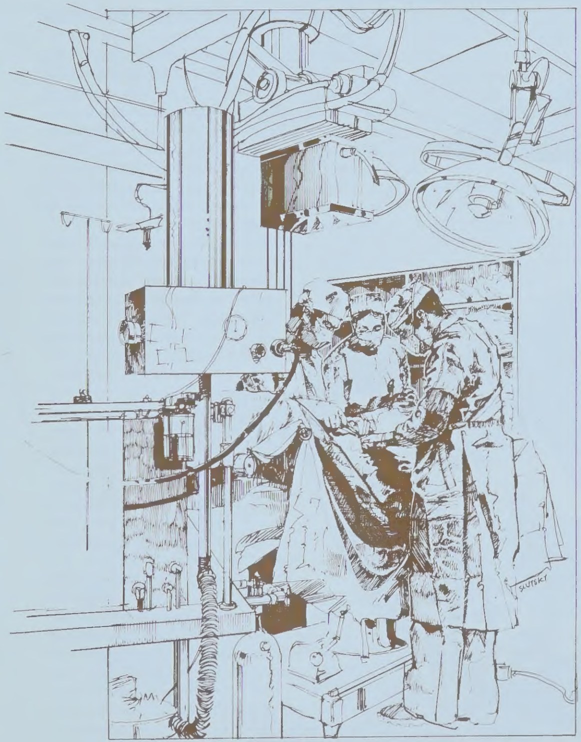
COMMUNITY HEALTH CARE SERVICES

The commitment to maintain high quality health care through a variety of programs and services remains the theme of Extendicare's philosophy. One important feature of a balanced, well-directed health care delivery system lies in its capability of providing community and residential, as an alternative to institutional, forms of care.

Through its subsidiary, Para-Med Personnel Services Ltd., Extendicare is increasingly involved in delivering an expanding range of health care services in many districts across Canada. For example, the company has been providing daily homemaker's services, such as housekeeping, meal preparation, personal hygiene and group excursions for shopping and recreation, for a group of physically disabled residents of an Ottawa rehabilitation project. It has also been providing a range of support services for a home care program in Metropolitan Toronto. It currently provides several hundred hours of services each week to these clients.

During the past year, we have been involved in a series of private and government surveys and projects to assess the specific health care needs of particular communities, citizen groups and institutions, with a view to helping fill these needs. Resulting programs include the provision of certain diagnostic, screening and other preventative health services to employees of various Southern Ontario industries, and the planning and staffing of a community diagnostic and urgent care centre.

In addition, the company works closely with organizations to develop in-service training programs, which include basic charting and communication, nutrition, body mechanics, patient hygiene, care of the handicapped, family living, child care, and accident prevention.



HEALTH CARE SUPPLIES

Hartz Standard, a division of Extendicare, is the largest Canadian medical and surgical supply distributor with coast-to-coast sales and distribution systems. With its purchases from a dozen different countries, Hartz Standard can fully equip a hospital with the supplies it needs, from operating room and intensive care equipment to furniture, patient handling equipment, and day-to-day medical and surgical supplies.

Hartz Standard's medical supply specialists have been invited to become part of a hospital's team, advising on new equipment, new applications of existing products, inventory and distribution systems and in-service training. More recently, the company has contracted with Canadian hospitals to be their prime vendor on a continuing basis, thus providing volume prices, reliable delivery, quality, products and balanced inventory control. The Prime Supplier Program, which the company helped pioneer, is another facet of our multi-unit management capability, where we contract with an organization to be its major supplier and materials management coordinator.

The division also completed the equipping of two medium sized general hospitals in eastern Canada, advising on the specifications, identifying suppliers, expediting delivery and overseeing installation of equipment.

HEALTH CARE OPERATIONS — UNITED STATES

HEALTH CARE FACILITIES

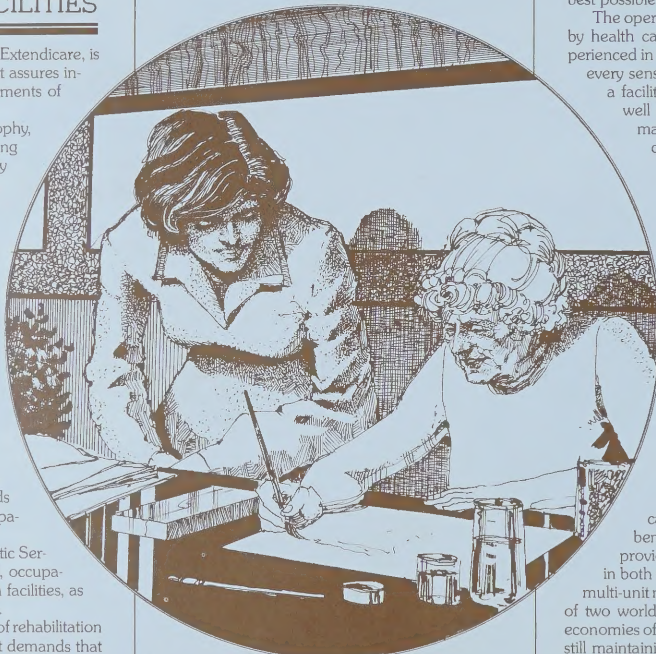
Medco Centers, Inc., a subsidiary of Extendicare, is committed to total resident care that assures individualized attention to the requirements of each resident.

The company's basic philosophy, upon which care programs in a nursing centre must be based, is that the facility is an integral part of the community and that each resident has unique physical, social, emotional and spiritual needs which must be met to attain the highest level of function and independence. A sense of security and belonging, coupled with dignity, comfort, and a positive outlook, are of prime importance. Medco communicates closely with physicians, residents and families, and continuously assesses the residents' progress and the effectiveness of therapy, activities, dietary and other programs.

Medco owns, leases or manages 26 nursing centres, with 2,459 beds and in fiscal 1978 provided 746,562 patient days of health care service.

Through its subsidiary, Therapeutic Services, Inc., Medco provides physical, occupational and speech therapy in its own facilities, as well as to others, including hospitals.

To achieve the optimum degree of rehabilitation and independence for each resident demands that every facility apply proven management systems to ensure that available dollars are being spent in the best possible way.



The operations of all our facilities are carried out by health care professionals, people who are experienced in the field and who ensure that service, in every sense of the word, is kept foremost. When a facility is well-managed administratively, as well as medically, care for residents automatically remains high and, in many cases, improves.

The company's management services for private organizations and governments are in growing demand. Providers of health care are increasingly contracting with a specialist team having specialized skills to assist in solving the complex management problems faced by the health care community as it strives to continue giving the best possible care. Medco, and its parent company, Extendicare, are a multi-unit management team with the resources, the information systems and the experience to work with administrators in meeting management challenges.

Extendicare's United States' health care facilities, like Canada's, enjoy the benefits of multi-unit management, which provides know-how and specialized services in both countries. We have demonstrated that multi-unit management offers institutions the best of two worlds — the opportunity to benefit from economies of scale and management expertise while still maintaining ownership, current administration, trustee autonomy and community involvement.

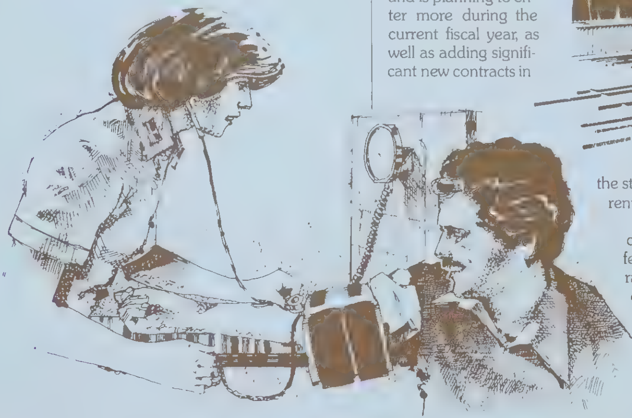
DIAGNOSTIC SERVICES

Preventive health care through diagnostics is encouraged by governments at all levels. Such care supports a reduction in the number of patient days in hospitals and leads to improved personal care. In the United States, Extendicare is meeting the growing need for preventive health care through two subsidiary companies.

United Health Maintenance, Inc., operates a fleet of mobile multi-phasic screening and testing units coast-to-coast. With a capability for the early detection of medical problems through a comprehensive group of tests and laboratory procedures, the accent is strongly placed on preventive care.

The 30-foot-vans of United Health Maintenance, staffed with skilled technicians and nurses and equipped with sophisticated equipment, bring medical tests to people in the community, at work and at school sites. In case of a major crisis or disaster, the mobile units can be converted to administer emergency care. The health care team in each van participates in a continuous program of learning the latest life-saving and emergency techniques.

During the year, United Health Maintenance extended its operations into additional states and is planning to enter more during the current fiscal year, as well as adding significant new contracts in the states where it currently operates.



The second Extendicare subsidiary is Professional Clinical Laboratories, Inc., the largest private diagnostic laboratory company in Delaware, with locations throughout the state, which has been in operation for over 10 years.

The company provides accurate, dependable services to patients, doctors, health care facilities and industries. Because time is all-important in diagnosis, Professional Clinical Laboratories maintains radio-dispatched vehicles for rapid pick-up and delivery of specimens.

In addition to its fixed facilities, the company provides technicians who go to the homes of non-ambulatory and confined patients to conduct screening services.

Professional Clinical Laboratories complements the company's United Health Maintenance operations and increases the availability of diagnostic services to a greater segment of the U.S. public.

BOARD OF DIRECTORS, OFFICERS AND ADVISORY PERSONNEL

extendicare ltd.

Shareholders are invited to attend the company's Annual Meeting at 10 a.m., March 26, 1979 in the Library Room of the Royal York Hotel, Toronto.

Board of Directors

Harold L. Livergant
Chairman of the Board and President

*James A. Bradshaw, Q.C.
Solicitor
Campbell, Godfrey & Lewtas

The Hon. Sidney L. Buckwold,
Senate of Canada

H. Michael Burns
Vice-Chairman
Crown Life Insurance Company Limited

*H. Hoyle Campbell, M.D.
Surgeon

William E. Hewitt
Manager, Financial Operations, Imperial Oil Limited

Eleanor McKinnon

*Derril G. McLeod, Q.C.
Solicitor
Pedersen, Norman, McLeod & Todd

Carole Pulver

J. Russell Scott, M.D.
Physician

Martin D. Shyba
Director and Executive Consultant

*Jean-Paul Tessier
President
BGL Construction Ltd.

*Executive Committee Member

Officers

Harold L. Livergant
Chairman of the Board and President

J. Wesley Carter
Executive Vice-President

Jacob Birbrager
Senior Vice-President, Engineering

Richard A. Gardner
Senior Vice-President, Administration

Jacques Krasny,
Senior Vice-President, Management and Development

Winston Ling
Senior Vice-President, Finance

Gerald P. Hiebert
Vice-President and General Manager, Canadian Health Care Division

Donald P. Schurman
Vice-President

Margaret MacKay
Assistant Vice-President

Richard G. Ponesse
Vice-President and General Manager, Hartz-Standard Division

Steven P. Currie
Treasurer

Michael R. Kordyback
Assistant Treasurer

Richard L. Bertrand
Controller

Benjamin J. Hutzel
Secretary

Medical and Technical Advisory Board

J. B. Campbell,
B.Sc., Ph.D.

C. J. Doherty,
M.D., F.A.C.C.P., F.A.G.S.

D. E. Hunt,
M.D., F.C.F.P.

W. Leers,
M.D., Ph.D., F.R.C.P.(C), Dip. Bact.

W. Harding LeRiche,
M.D., M.P.H., F.R.C.P.(C)

L. W. MacPherson,
M.R.C.V.S., D.V.S.M., Ph.D.

R. K. Murray,
M.B., Ch.B., M.S., Ph.D.

P. K. O'Brien,
M.B., F.R.C.P.(C), M.R.C.(PATH)

F. Burns Roth,
M.D.

L. Roth-Moyo,
B.Sc., M.D., F.R.C.P.(C)

E. C. Shortliffe,
M.D., F.A.C.H.A.

F. O. Wishart,
M.D., D.P.H., C.R.C.P.

J. S. Wootliff,
F.R.C.P.(C), M.B., M.R.C.(PATH)

Transfer Agents for Class A and Common Shares

Montreal Trust Company

Auditors

Thorne Riddell & Co.

Legal Counsel

Campbell, Godfrey & Lewtas

Principal Banker

Bank of Montreal

CORPORATE DIRECTORY

CANADIAN HEALTH CARE DIVISION

VICE-PRESIDENT AND GENERAL MANAGER:
GERALD P. HIEBERT
VICE PRESIDENT:
DONALD P. SCHURMAN
ASSISTANT VICE-PRESIDENT:
MARGARET MacKAY
Head Office: 1 Yonge Street, Suite 900,
Toronto, Ontario M5E 1E5.
Telephone (416) 361-0572.

Skilled nursing centres, owned and operated by Extendicare:

ONTARIO

Haliburton
Kingston
London
Mississauga
Oakville
Oshawa
Ottawa — Medex
Ottawa — New Orchard
Ottawa — Starwood
Peterborough
Port Stanley
St. Catharines
Sudbury
Toronto — Highbourne
Toronto — North York
Toronto — Scarborough

SASKATCHEWAN

Moose Jaw
Regina — Parkside
Regina — Rae Street
Regina — Sunset Drive
Saskatoon

Skilled nursing centres, managed by Extendicare:

Country Village Incorporated, Woodslee, Ontario
Hyde Park Nursing Home Ltd., Guelph, Ontario.
Tendercare Nursing Homes Ltd., Sault Ste. Marie, Ontario.
Frank Eliason Centre, Saskatoon, Sask. (hospital)

Diagnostic Services

DIRECTOR: DAWN J. JEFFERY
TECHNICAL DIRECTOR: ALEX SESLER
4949 Bathurst Street,
Toronto, Ontario M2R 1Y1.

Telephone: (416) 223-9575.

12 locations in Metropolitan Toronto.

Para-Med Personnel Services Ltd.

ACTING DIRECTOR: HELEN TAPE
Head Office: 55 Queen Street East, Suite 704,
Toronto, Ontario M5C 1R6.
Telephone: (416) 864-9575.

Branch offices in:

London, Hamilton, Kingston, Ottawa.

HARTZ-STANDARD DIVISION

VICE-PRESIDENT AND GENERAL MANAGER:
RICHARD G. PONESSE
Head Office: 24 Metropolitan Road,
Scarborough, Ontario M1T 2T8.
Telephone (416) 291-5541.

Division offices in:

Vancouver
Calgary
Saskatoon
Winnipeg
Scarborough
Toronto (Retail Store)
Ottawa
Montreal
Dartmouth, N.S.
St. John's, Nfld.

MEDCO CENTERS, INC.

VICE-PRESIDENT AND GENERAL MANAGER:
WILLIAM T. GALA
DIRECTOR OF FINANCE: ROBERT JOBES
DIRECTOR OF OPERATIONS: WAYNE MAYO
Head Office: 405 Carpenter Street,
Evansville, Indiana 47703.
Telephone: (812) 422-3231.

Nursing homes owned or leased by Medco:

INDIANA

Chandler
Elkhart
Evansville
Evansville — North
McCurdy Residential
Newburgh
French Lick
Medco Annex
Medco Centre
Huntingburg
Loogootee
Mount Vernon

KENTUCKY

Bowling Green
Brandenburg
Campbellsville
Elizabeth Town
Fordsville
Frankfort
Franklin
Hardinsburg
Henderson
Morganfield
Owensboro
Paducah
Pembroke
Springfield

Nursing homes managed by Medco:

Clarksville, Indiana
Danville, Indiana.

UNITED HEALTH MAINTENANCE, INC.

PRESIDENT: KENNETH L. BLUM
Head Office: 9017 Red Branch Road, Suite 203
Columbia, Maryland 21045.
Telephone: (301) 730-9009.

Area Offices:

Washington, D.C.
Atlanta, Georgia
Hartford, Connecticut
Buena Park, California
Los Angeles, California

PROFESSIONAL CLINICAL LABORATORIES, INC.

VICE PRESIDENT AND GENERAL MANAGER:
EDGAR N. ADAMS
DIRECTOR OF MARKETING: LEO LONG
TECHNICAL DIRECTOR: ROSE HILGER
Head Office: 1701 Shallcross Avenue,
Wilmington, Delaware 19806.
Telephone: (302) 575-0570.

CONSOLIDATED BALANCE SHEET

as at August 31, 1978

extendicare ltd.

(Incorporated under the laws of Canada)

ASSETS

	1978	1977
CURRENT		
Accounts receivable	**$10,267,812**	$ 8,088,666
Inventories (note 3)	**6,363,890**	6,588,092
Prepaid expenses and deposits	**853,028**	751,004
Trust funds held for residents	**338,780**	333,080
	17,823,510	15,760,842
PROPERTY AND EQUIPMENT (note 4)	**42,420,634**	40,911,478
OTHER		
Other assets (note 5)	**2,073,460**	2,121,517
Deferred charges, less amortization	**645,537**	682,358
Deferred foreign exchange adjustment	**1,211,197**	502,296
Goodwill (note 6)	**5,740,088**	4,879,063
	9,670,282	8,185,234
	$69,914,426	$64,857,554

Approved by the Board

Director

Director

LIABILITIES

	1978	1977
CURRENT		
Bank indebtedness (note 7)	**$ 1,946,388**	$ 4,347,805
Accounts payable and accrued liabilities	**7,910,711**	6,559,114
Income taxes payable	**577,039**	52,071
Principal due within one year on non-current liabilities	**3,099,328**	2,481,809
Deferred income taxes	**806,396**	658,217
Trust funds held for residents	**338,780**	333,080
	14,678,642	14,432,096
NON-CURRENT LIABILITIES (note 7)	**34,050,116**	33,671,482
DEFERRED INCOME TAXES	**2,828,903**	2,659,558
MINORITY INTEREST	**484,956**	401,450

SHAREHOLDERS' EQUITY

CAPITAL STOCK (note 8)		
Authorized		
4,000,000 Common shares without nominal or par value		
500,000 Preferred shares of the par value of $10 each		
Issued and fully paid		
2,172,689 Common shares (1977 — 2,048,678 common shares)	**6,773,307**	5,867,837
Amount for which common shares are to be issued (note 2)	**825,600**	
	7,598,907	5,867,837
RETAINED EARNINGS (note 8)	**10,272,902**	7,825,131
	17,871,809	13,692,968
	$69,914,426	$64,857,554

Commitments, contingent liabilities and subsequent events (notes 11, 12 and 13)

CONSOLIDATED STATEMENT OF EARNINGS

Year ended August 31, 1978

	1978	1977
REVENUE		
Skilled nursing centres	**$52,511,850**	$42,007,864
Medical, surgical, pharmaceutical supplies and equipment	**26,800,787**	23,049,244
Diagnostic centres and other	**8,008,216**	6,117,376
	87,320,853	71,174,484
COSTS AND EXPENSES		
Operating	**67,266,284**	55,147,558
Administrative and general	**8,498,664**	5,770,772
Interest on non-current liabilities	**3,433,654**	3,296,409
Depreciation	**1,792,156**	1,562,854
Amortization of deferred charges and goodwill	**314,022**	126,796
	81,304,780	65,904,389
EARNINGS BEFORE THE UNDERNOTED	**6,016,073**	5,270,095
INCOME TAXES		
Current	**2,526,678**	2,071,190
Deferred	**276,068**	416,662
	2,802,746	2,487,852
EARNINGS BEFORE MINORITY INTEREST	**3,213,327**	2,782,243
Minority interest	**75,275**	92,558
NET EARNINGS	**$ 3,138,052**	$ 2,689,685
EARNINGS PER SHARE (note 9)	**$1.52**	$1.32

CONSOLIDATED STATEMENT OF RETAINED EARNINGS

Year ended August 31, 1978

	1978	1977
BALANCE AT BEGINNING OF YEAR	**$ 7,825,131**	$ 5,705,915
Net earnings	**3,138,052**	2,689,685
	10,963,183	8,395,600
Dividends	**690,281**	570,469
BALANCE AT END OF YEAR	**$10,272,902**	$ 7,825,131

CONSOLIDATED STATEMENT OF CHANGES IN FINANCIAL POSITION

Year ended August 31, 1978

	1978	1977
WORKING CAPITAL DERIVED FROM		
Operations	**$ 5,455,874**	$ 4,693,943
Proceeds from sale of assets, net of mortgage receivable taken back	**314,675**	139,212
Non-current liabilities assumed	**2,473,212**	4,636,374
Issue of shares		
For cash on exercise of stock options and warrants	**770,011**	39,957
On conversion of notes	**135,459**	109,410
	9,149,231	9,618,896
WORKING CAPITAL APPLIED TO		
Additions to property and equipment	**2,797,660**	1,706,341
Acquisition of businesses, plus working capital deficiency in 1978 of $300,880 (note 2)	**572,180**	1,467,440
Dividends	**690,281**	570,469
Reduction in non-current liabilities	**2,983,268**	5,256,237
Purchase of minority interest in Medco Centers, Inc.		370,992
Other items	**289,720**	389,139
	7,333,109	9,760,618
INCREASE (DECREASE) IN WORKING CAPITAL	**1,816,122**	(141,722)
WORKING CAPITAL AT BEGINNING OF YEAR	**1,328,746**	1,470,468
WORKING CAPITAL AT END OF YEAR	**$ 3,144,868**	$ 1,328,746

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Year ended August 31, 1978

1. SUMMARY OF ACCOUNTING POLICIES

The major accounting policies of Extendicare Ltd. and subsidiary companies are set out below. These policies are in accordance with generally accepted accounting principles and have been consistently applied.

(a) Principles of consolidation

The consolidated financial statements include the accounts of all subsidiary companies. Principal subsidiaries which are not 100% owned are Medco Centers, Inc. (94%) and United Health Maintenance Inc. (80%).

Earnings from businesses purchased or sold are included from or to the effective dates of their purchase or sale.

(b) Translation of accounts into Canadian dollars

The accounts for foreign operations included in the consolidated balance sheet are translated at year end rates of exchange except that (a) property and equipment, deferred charges and accumulated depreciation and amortization are at rates at dates of acquisition and (b) deferred income taxes are at the rate used to translate the assets and liabilities to which they relate. The accounts for foreign operations included in the consolidated statement of earnings except depreciation, amortization and deferred income taxes are translated at average rates of exchange during the year.

The Company has for the most part borrowed funds to acquire and finance foreign operations in the same currency in which such operations are carried on and accordingly it is expected that borrowings will be repaid out of funds generated in the same currency. The Company believes that it could be misleading to recognize immediately all translation gains or losses which arise from fluctuations in exchange rates. Accordingly, the net difference on translation at current rates of exchange of other assets and non-current liabilities from that in effect at the date of acquisition or origin has been deferred until realized and is shown on the balance sheet as "Deferred foreign exchange adjustment".

(c) Inventories

Inventories are valued at the lower of cost and net realizable value.

Cost is determined by the first in first out method. Net realizable value for resale merchandise is the selling price of the product less provision for normal selling costs.

(d) Property and equipment

Property and equipment is stated at historical cost. Provisions for depreciation are computed by either the straight line method or declining balance method at rates based on the following estimated life expectancies:

Buildings	— 20 to 40 years
Furniture and equipment	— varying periods not exceeding 20 years
Leasehold improvements	— the term of the applicable leases.

The related leasehold interest included in other assets is stated at cost and is amortized on a straight line basis over the term of the lease.

(e) Deferred charges

It is the policy of the Company to defer revenues and operating expenses of new nursing centres and new division operations until such time as they are deemed operational. They are deemed to be operational in the month during which revenues equal or exceed expenses or one year from the date revenue is first earned, whichever first occurs. Net amounts deferred are then charged to earnings over three to five years on a straight line basis.

Direct loan costs are also deferred and amortized over the life of the related debt.

In addition, certain market development costs have been deferred and are being amortized over varying periods up to five years.

(f) Goodwill

Goodwill arises from the excess of purchase price for businesses over the fair value of assets acquired at the dates of acquisition. It may arise either through the purchase of assets or shares of a business.

Goodwill acquired subsequent to April 1, 1974 is amortized to earnings on a straight line basis, presently over forty years. Goodwill acquired prior to that date is carried in the accounts at cost without amortization.

(g) Income taxes

Income taxes charged in the consolidated statement of earnings represent both the portion currently payable and the portion which is deferred. The deferment of income taxes results from claiming depreciation and other items for tax purposes in amounts which differ from those recorded

in the accounts and from filing certain U.S. federal income tax returns on a cash basis while the financial statements recognize revenues and expenses on an accrual basis.

(h) Revenue

The fees charged by the Company for its nursing home facilities and diagnostic services in Canada are subject to the regulated rate structures determined by the respective provincial authorities. Such regulation has been and is provided by the establishment of maximum rates for the industry rather than for individual entities within the industry.

The fees charged by the Company for its nursing home facilities in the United States include revenues resulting from residents participating in federal and state funded cost reimbursement programmes. These revenues are based on the approved prospective rates which were in effect from time to time during the period. Final cost settlement adjustments, if any, are recorded when objectively determinable.

2. ACQUISITION

Effective July 1, 1978, the Company acquired 100% of the outstanding shares of Professional Clinical Laboratories, Inc. which operates laboratories in the state of Delaware.

This transaction has been accounted for by the purchase method.

Details of the transaction are as follows:

Net assets acquired at value assigned thereto		
Current assets	$ 415,950	
Property and equipment	780,780	
Goodwill	890,600	$2,087,330
Current liabilities	716,830	
Non-current liabilities	273,600	990,430
		$1,096,900
Consideration given		
Cash		$271,300
Value attributed to common shares issued on closing, September 28, 1978		825,600
		$1,096,900

The Company may be required to issue up to 16,683 additional common shares in connection with this acquisition if revenues of Professional Clinical Laboratories, Inc. exceed specified levels in 1979.

3. INVENTORIES

	1978	1977
Resale merchandise	**$5,465,398**	$5,807,060
Supplies	**898,492**	781,032
	$6,363,890	$6,588,092

4. PROPERTY AND EQUIPMENT

	1978	1977
Land	**$ 3,807,149**	$ 3,434,225
Buildings	**34,754,575**	33,427,000
Furniture and equipment	**8,670,480**	7,649,865
Leasehold improvements	**722,245**	491,085
	47,954,449	45,002,175
Accumulated depreciation	**7,282,598**	5,640,199
	40,671,851	39,361,976
Land, option, plans and construction in process re future facilities	**1,748,783**	1,549,502
	$42,420,634	$40,911,478

5. OTHER ASSETS

	1978	1977
Long term portion of mortgages and notes receivable	**$ 884,241**	$ 1,155,152
Loans to officers, secured	**813,500**	334,375
Leasehold interest, less amortization	**312,565**	332,406
Sundry, at cost	**63,154**	125,769
Land, buildings and related assets of facility subject to sale agreement, at cost		173,815
	$ 2,073,460	$ 2,121,517

6. GOODWILL

	1978	1977
Purchased goodwill (purchase of assets)	**$ 2,802,228**	$ 2,695,803
Excess of purchase price of shares of certain subsidiary companies over fair value of assets acquired (purchase of shares)	**2,937,860**	2,183,260
	$ 5,740,088	$ 4,879,063

7. BANK INDEBTEDNESS AND NON-CURRENT LIABILITIES

	1978	1977
The Company:		
First mortgages, 7-3/8% to 11-1/4% maturing through to 2007	**$17,513,668**	$17,696,920
Second mortgages, 9% to 11% maturing through to 1983	**1,033,587**	1,198,643
8-1/2% Sinking Fund Debentures, due 1984	**1,768,000**	2,034,000
Bank term loan at an interest rate varying with bank prime (including U.S. $1,400,000)	**2,096,000**	500,000
Promissory notes, 6-1/2% to 8% maturing through to 1981	**225,445**	566,729
Canadian Subsidiaries		
First mortgage, 11-3/4% maturing 1981	**707,652**	713,731
Notes payable to minority shareholder, non-interest bearing	**26,360**	26,360
United States Subsidiaries		
Mortgages payable, 6% to 10-1/4% maturing through to 1996 (U.S. $4,411,783)	**5,029,433**	4,323,066
Notes payable, 3% to 10.84% maturing through to 1983 (U.S. $2,119,310)	**2,416,015**	2,846,529
Lease purchase and sales contracts payable, various rates to 11% maturing through to 1993 (U.S. $2,155,512)	**2,457,284**	2,592,313
Bank term loan, at an interest rate varying with New York bank prime, maturing through to 1983 (U.S. $3,400,000)	**3,876,000**	3,655,000
	37,149,444	36,153,291
Less principal due within one year and included in current liabilities	**3,099,328**	2,481,809
	$34,050,116	$33,671,482

The weighted average annual interest rate of all non-current liabilities is approximately 10.1%.

Substantially all assets of the companies are mortgaged or pledged as security for bank indebtedness or non-current liabilities.

Principal payments on non-current liabilities due within the next five fiscal years after giving effect to renewal privileges are as follows:

1979	$3,099,328
1980	4,577,357
1981	4,610,384
1982	1,923,097
1983	2,269,277

8. SHAREHOLDERS' EQUITY

During the year 12,950 common shares were issued for $72,511 cash on exercise of stock options, 18,061 common shares were issued on conversion of $135,459 convertible notes and 93,000 common shares were issued for $697,500 cash on exercise of warrants.

Restrictions under the trust indenture securing the 8-1/2% Sinking Fund Debentures prohibit the payment of dividends which would reduce shareholders' equity, as defined in the trust indenture, below $3,000,000.

Under a bank debenture the Company has agreed, unless otherwise consented to by the bank, to restrict dividends to 50% of the Company's net earnings for the year. The dividends currently being paid by the Company are well within the maximum established by this debenture.

The company has 169,700 common shares reserved for issue upon exercise of outstanding warrants at $7.50 per common share to May 15, 1979, when the warrants expire.

In addition 100,000 common shares were originally reserved for issuance to officers and key employees under the Company's Incentive Stock Option Plan, of which 43,550 shares have been exercised to August 31,1978. At August 31, 1978, 19,800 shares were optioned to officers and 16,859 shares to other employees at prices ranging from $3.75 to $8.50 with varying expiry dates to January, 1983.

9. EARNINGS PER SHARE

Earnings per share have been calculated on the weighted average number of shares outstanding during the year.

Fully diluted earnings per share are $1.36 for the year ended August 31, 1978. Fully diluted earnings per share have been calculated on the basis of exercising at the beginning of the year all rights and options and imputing earnings of $88,000 after tax, on the cash to be received which would have been used to retire certain indebtedness.

10. OTHER STATUTORY INFORMATION

	1978	1977
Number of directors	**12**	11
Aggregate remuneration of directors as directors	**$ 18,000**	$ 10,500
Number of officers	**10**	12
Aggregate remuneration of officers as officers	**$402,624**	$371,425
Number of officers who were also directors	**1**	2

11. LONG TERM LEASES

The Company has lease commitments with terms expiring up to 2003, exclusive of renewals. Maximum rentals to be charged to earnings are as follows for each of the periods shown after giving effect to the purchase on September 1, 1978 of a nursing home previously leased (see note 13).

For the year:	1979	$ 1,143,562
	1980	1,036,599
	1981	959,862
	1982	896,847
	1983	790,630
For the following:		
	1984 to 1988	2,892,075
	1989 to 1993	1,690,873
	1994 to 1998	168,340
	1999 to 2003	55,240
		$9,634,028

During the year ended August 31, 1978 rent expense of $1,519,866 has been charged to operations.

12. CONTINGENT LIABILITIES

(a) The Company is liable as an original guarantor in respect of a first mortgage on the nursing home sold by a subsidiary during 1976. The principal balance outstanding under this mortgage at August 31, 1978 was approximately $1,540,000.

(b) In connection with an agreement to manage two nursing homes in the State of Indiana in the United States, the Company agreed in 1976 to guarantee the obligations of the purchaser of the two homes, and its parent corporation, in respect of both a first mortgage of which U.S. $285,000 was outstanding at August 31, 1978 and a long term lease requiring minimum annual payments of approximately U.S. $75,000 and terminating in 1999. The management agreement, at the option of the Company, is to remain in effect until it has no further obligation under either the mortgage or the lease.

(c) The Company, under certain circumstances, may be required to acquire at a price based upon a multiple of earnings, a portion or all of the remaining 20% minority interest in United Health Maintenance, Inc.

13. SUBSEQUENT EVENTS

(a) On September 1, 1978, the Company exercised an option and acquired for $2,724,000 a nursing home facility which was previously leased. Consideration for the acquisition was cash and the assumption of an existing first mortgage in the amount of $2,136,000.

(b) On December 11, 1978 the shareholders of the Company at a special general meeting passed a special resolution authorizing the directors to apply for a certificate of continuance continuing the Company under the Canada Business Corporations Act and amended its letters patent. As a result, after continuance the authorized capital of the Company will consist of:

(i) an unlimited number of preferred shares without nominal or par value, issuable in series;

(ii) an unlimited number of non-voting Class A shares without nominal or par value ("Class A Shares"); and

(iii) an unlimited number of convertible common shares without nominal or par value ("Common Shares").

The previously authorized but unissued preferred shares of the par value of ten dollars ($10) each and the previously authorized but unissued common shares without nominal or par value will be cancelled and each

of the previously issued and outstanding common shares without nominal or par value will be sub-divided into one Class A Share and one Common Share.

The Class A Shares and the Common Shares, replacing the Company's existing common shares, will be similar to each other in all respects except that:

(i) the Class A Shares will be non-voting while the Common Shares will be voting:

(ii) the Class A Shares will entitle the holders thereof to non-cumulative dividends totalling 10¢ per share in each financial year of the Company (if and when declared by the directors) in priority to any dividends on the Common Shares;

(iii) after the preferential dividends on the Class A Shares referred to in (ii) have been declared in each financial year of the Company and their payment authorized within such financial year, the Class A Shares and Common Shares will participate equally share for share in all further dividends during such financial year; and

(iv) the Common Shares will be convertible into Class A Shares on a one for one basis but the Class A Shares will not be convertible into Common Shares.

AUDITORS' REPORT

To the Shareholders of Extendicare Ltd.

We have examined the consolidated balance sheet of Extendicare Ltd. as at August 31, 1978 and the consolidated statements of earnings, retained earnings and changes in financial position for the year then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests and other procedures as we considered necessary in the circumstances.

In our opinion, these consolidated financial statements present fairly the financial position of the company as at August 31, 1978 and the results of its operations and the changes in its financial position for the year then ended in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

Toronto, Canada
November 13, 1978
(December 11, 1978 as to note 13(b))

Thorne Riddell & Co.
Chartered Accountants